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General Business Conditions

THE business situation has shown little change during the past month. The most conspicuous development is the flattening out of the commodity price advance, due mainly to further declines in agricultural prices. However, little effect of these declines is to be seen in reports of trade or production. Merchandise sales on the whole continue to show satisfactory increases over a year ago. Industrial production, recovering from a dip during the vacation season, holds close to the ceiling, with the industries in the aggregate turning out about all that the supply of labor and materials will permit. Nor is there reason to expect an early change in industrial activity or employment. In some lines the "catching up" period is over and moderate curtailment is in effect, but the slackening counts for little in the overall picture. In such major industries as metals, automobiles, petroleum, most types of construction, railway, utility, and farm equipment, and a good many others, the business on

hand or in sight will support the present rate of output — or a higher rate if it could be reached — for many months to come.

The principal effects of the farm price declines and the evidences of "catching up" seem to be on sentiment rather than on trade. Only two months ago the headlines were full of the inflation problem. Congress was called into special session to deal with it. President Truman warned of collapse unless his demands for more government controls were granted. For a time an atmosphere of crisis was created, which led many people to feel that inflationary forces were in full control, that living costs would keep on rising and the wage-price spiral turning, and that drastic restrictive measures were justified.

A Swing in Sentiment

In two months, the change of sentiment has been marked. Even while emergency action was being demanded, the crops were getting almost ideal weather and estimates of yields were being raised to phenomenal figures. The factories and mills were rolling out goods, and more and more distribution channels and consumers' closets were filling up. Since the Congressional session the influence of these factors on prices has become more effective. The rise in the wholesale commodity price index has given way to a sidewise trend, the headline emphasis on inflation has abated, and the views of those who expect deflation and recession are again commanding attention and influencing business opinion. Probably any poll taken today would show a very considerable belief that the country is passing through the peak of the boom and of the price rise, with a downtrend in sales and eventually in manufacturing activity to follow. The stock market has been on the easy side, and the National Association of Purchasing Agents comments on the tendency of industrial buyers to shorten further their already short commitments. It says

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60 per cent are keeping their coverage down to 60 days or less.

Sentiment usually swings to extremes, and the present swing may be greater than is warranted by changes in actual conditions in this brief time. Underlying it, however, is the distrust of the outlook which has been evident, and which at intervals has risen to the surface, throughout the past two years. Many expected declines in industrial production before the end of 1947, only to have to move the date ahead to 1948, and now to 1949. They expected, and rightly, that some of the soft goods particularly would catch up with accumulated needs and face curtailment. They expected the upsurge of costs and prices to narrow the markets by shutting out buyers whose incomes lagged. They also expected, and rightly, that buying for inventory would fall off as pipelines filled. They were concerned about the fundamental weaknesses that develop during inflation, the growth of debt, waste and inefficiency. Many believed not only that boom must be followed by bust, but also that the bust could not be much longer deferred.

Paradoxically, lack of confidence in the soundness of the business situation has contributed something toward keeping it sound. Caution helps to maintain orderly markets and minimize speculative excesses, extravagance and over-expansion. In the end it helps prolong activity. The conservatism and sound sense of the business community, which ironically has been fortified by fear that a bust was around the corner, has been a stabilizing and supporting influence on business throughout the two years.

Inflationary Pressures Still Present

Although passage of time and the gigantic production of the farms and factories are bringing stabilizing forces into play, any analysis of the outlook must also take account of the inflationary forces and their supporting effects. The decline in farm prices automatically brings new inflationary expenditures, made by the Government in loans and purchases to support the farm markets, into the income stream. As described in a subsequent article, the Treasury will be diverting vast sums, which otherwise might be applied to checking inflation by reducing the government debt, into the farmers' hands. Farm income and purchasing power will be supported accordingly.

The wheat farmers will have less money than last year, both because the crop was slightly smaller and the price lower. Cotton farmers, however, will have a half billion dollars greater cash income than in 1947, by selling a larger crop

in a supported market. The record-breaking corn crop will be sold on more favorable terms than the corn price itself indicates, because most of it will move to market in the form of livestock or animal products, selling at high prices relative to corn. Prices of oilseeds will average lower than last year despite support of flaxseed at \$6 a bushel again, but the crops are substantially larger.

Moreover, a modest decline in farm income cannot affect farm purchasing power as did the drop in 1920, for example, since farmers have unparalleled resources in cash and war bonds and relatively small debts. On January 1, 1948 farmers' liquid assets exceeded \$22 billion and their debts were \$9 billion. Their liquid assets were 2½ times their debts, whereas before the war their debts were 2½ times their liquid assets. This store of savings justifies them in spending current income freely and gives them the means to buy the equipment and other goods they have been waiting for. Meanwhile city people will not have to allot quite as much of their income for the purchase of farm products. They are getting cotton goods and a few foods at lower prices now, and as time goes on they can expect to buy other clothing and foods more cheaply.

Deflation and Its Offsets

Most observers expect business spending, particularly on plant, to decline in 1949. Again an inflationary offset is present, in the prospect of greater spending by state and local governments, on highways, and in federal expenditures for defense, which will be higher in this fiscal year than last year, and higher next year than this.

Exports have declined some 30 per cent, at an annual rate, from the peak reached in the spring of 1947. This drop is already in the current figures of gross national product and national income, and although some forecasters expected it to have a depressing effect when it came, it has been taken in stride. From now on disbursements under the European Recovery Program will increase and sustain the export level.

The situation in the metals continues strong, but if it should weaken the Government will give support in this area also, through purchases under the program of stockpiling strategic materials.

Finally, present credit policy keeps the doors of Federal Reserve credit open to holders of government bonds, and is a cushion against drastic deflation of either the bond market or the money supply. This policy is inflationary. Whether it is dangerously so is a matter upon which opinions

differ and debate is now raging. All can agree, however, that it provides general support against deflationary influences.

Effect of Supports

Existence of these supports warrants two conclusions. The first is that complacency with respect to inflationary dangers is hardly justified. Price supports and huge government programs of spending-lending-guaranteeing are inflationary. Although both sentiment and events have lately swung toward the deflationary side, there is no guarantee that they will not swing the other way again. The second conclusion is that the belief that the boom must end in violent collapse ought to be carefully examined in light of the supports enumerated. The historical precedents are all against stabilization at levels reached during a boom, or even approximately so. But there are no precedents for a situation in which public policy provides props, in part automatically, as recession sets in.

Of course consideration of what these government props may mean in the immediate business outlook should not imply that they point out a road to lasting stabilization and genuine economic progress. Necessary as the armament expenditures are for the country's protection, they are a drain upon the country's living standards, for they take labor and materials away from the production of goods which would raise living standards. Beneficial as E.R.P. may be in total, it also is a draft upon production which otherwise would be devoted to our own needs. These and other supports prop up business as long as they last, but whether paid for by taxation or inflation the cost is heavy and the ultimate effect in promoting boom and bust is incalculable. However, they will play a significant part in the business situation over the next year, either by keeping the inflation going or by cushioning recession in the private segment of the economy.

Increases in Reserve Requirements

Following in swift succession the moves announced in August to raise short-term interest rates and to curb the rise in consumer instalment credit, the Federal Reserve Board on September 8 ordered increases in bank reserve requirements of two points on demand deposits and one and one-half points on time deposits. The effective dates for the higher requirements, which apply to the 6,900 banks which are members of the Federal Reserve System, were set at September 16 for "country" banks, and at September 24 for

banks in the "central reserve" and "reserve city" classifications. There was an element of surprise in the timing since it had been quite generally expected that the authorities might delay action of this kind until the Treasury's September 15 and October 1 refundings, and the September tax collections, were out of the way.

In raising reserve requirements, as in the reimposition of instalment credit controls, the Reserve Board made further use of the powers granted in the Congressional Joint Resolution of August 16. Full use has now been made of the new authority to raise reserve requirements against time deposits, while half of the new power to lift the percentages against demand deposits has been exhausted. The move was announced "as a further step toward restraining inflationary expansion of bank credit." The following table shows the reserve requirement percentages now in effect, those previously in effect, and the amounts of funds involved for each class of member banks.

Member Bank Reserve Requirements

	Previous required percentage	New required percentage	Amount involved in increases*
On net demand deposits			
Central reserve city banks	24	26	\$ 490 million
Reserve city banks	20	22	570 "
"Country" banks	14	16	500 "
On time deposits			
Central reserve city banks	6	7½	40 "
Reserve city banks	6	7½	170 "
"Country" banks	6	7½	220 "
			\$1,990 "

* Based on average deposit volumes prevailing in the second half of July, 1948.

The total amount involved — about \$2 billion — is more suggestive of the magnitude of the increases than are the figures of 2 and 1½ percentage points. To require the member banks, by sudden edict, and on ten or fifteen days' notice, to raise \$2 billion additional cash to place on deposit with the Federal Reserve Banks, is no small order. Under ordinary circumstances it would require banks severely to prune down new lending as well as to sell off many of their government security holdings. The circumstances, of course, are not "ordinary". As it turned out, the announcement precipitated an avalanche of liquidation of government securities. These the Federal Reserve Banks bought and thus at once eased the problem of the banks in raising additional reserves and forestalled any general shutdown in the supply of credit. The seasonal uptrend in business loans on the books of the weekly reporting member banks, indeed, continued without significant change in the two weeks immediately following the announcement.

For this result, and for the continuing easy availability of long-term credits through insurance companies and other nonbank lenders, the vast purchases of government securities by the Federal Reserve Banks held the key. The following table reveals the expansion of the Federal Reserve government security portfolio, mostly notable in the bond account, between September 8, when the requirement increases were announced, and September 29, when the higher requirements were fully effective:

Federal Reserve Operations in Government Security Market
(In Millions of Dollars)

	Holdings		Change
	Sept. 8	Sept. 29	
Treasury bills	6,661	6,975	+ 314
Certificates of indebtedness	4,927	5,162	+ 235
Notes	1,785	1,948	+ 163
Bonds	7,864	9,202	+ 1,338
Totals	21,240	23,282	+ 2,042

Source: Weekly Federal Reserve statements.

Bank Portfolio Adjustments

While the authorities allowed prices of some of the bank eligible bonds to sag slightly below the minimum support levels established last Christmas Eve, the banks were major sellers of such bonds as well as of short-term Treasury obligations such as Treasury bills and certificates. Sales of bonds, of course, involved larger losses of current income than sales of short-terms, and often losses from price depreciation. On the other hand, sales of bonds afforded protection against the contingency of an adverse change in the official price support levels as well as against the contingency of increased loan demands from customers.

Bank selling, however, accounted for only a part of the Treasury bonds acquired by the Federal Reserve Banks during the rush of selling which followed the announcement of the reserve requirement increases. This conclusion is supported by a comparison of changes in bond holdings of the weekly reporting member banks in leading cities throughout the country with changes in bond holdings of the Federal Reserve Banks. Figures are not yet available for the weekly reporting member banks for September 29, but between September 8 and September 22—the first two weeks following the announcement and the period of heaviest Federal Reserve purchases—bond holdings of the weekly reporting member banks were reduced \$467 million. A good part of this decline represented redemptions of a maturing bond issue on September 15, rather than sales of bonds to the Federal Reserve Banks. In the same two weeks' period, the Federal Reserve Banks purchased \$1079 million Treasury bonds.

The Bond Support Operation

The accelerated purchases of government bonds by the Federal Reserve Banks naturally attracted attention and became the subject of increasing discussion and controversy. They created nervousness on the part of investment institutions quite generally and on the premise that the price-pegging program was in danger of breaking down under its own weight—in parallel to the British experience two years ago.

The discussions centered around the long-term bonds, which show up in the weekly Federal Reserve statement in the classification, "government securities over five years to maturity." The long-terms are the bonds which involve the greatest potential risk of market depreciation, and they include the restricted War Loan 2½s and 2½s to which official price support has been given most persistently, inflexibly and generously. They have been, for nearly a year, the hard core of the problem of bringing and holding the total Federal Reserve portfolio of government securities under control.

The following table, constructed from Treasury and Federal Reserve reports, shows the month-to-month pattern of selling by holders of long-term Treasury bonds as measured by purchases of bonds maturing after September, 1953, or after five years from the present date, by Federal Reserve Banks and government trust funds. Except for September, the purchases are broken down between "bank eligible" bonds, or those bonds on which no ownership restrictions are placed, and the "restricted" War Loan 2½s and 2½s which the banks are not eligible to buy. The figures for July, August, and September are tentative estimates based principally on the weekly Federal Reserve statements.

Official Purchases of Marketable Treasury Bonds
Maturing after September 15, 1953
(In Millions of Dollars)

	Bank Restricted Bonds	Bank Eligible Bonds	Total
1947			
November	199	198	397
December	1076	1118	2194
1948			
January	1356	294	1650
February	803	112	915
March	205	0	205
April	10	24	34
May	1	57	58
June	21	31	52
July	550e	*	550e
August	1000e	*	1000e
September	n.a.	n.a.	1800e

Italics indicate bonds sold out of official accounts and absorbed in the market.

* There was little or no evidence in the market for support for bank eligible bonds in July and August. e Estimated. n.a. Not available.

As the table indicates, price-supporting purchases from the beginning in November, 1947

through March, 1948 ran well above \$5 billion. After a brief interlude, liquidation was renewed toward the end of June and the total for this second wave was, at the end of September, beyond the \$2½ billion mark. The total for the entire eleven months is \$8 billion.

Of the long-term bonds acquired by the Reserve System and the government trust funds in the first wave of liquidation, November through March, two-thirds were restricted bonds and one-third bank eligible bonds. After the "Christmas Eve" drop in the government bond price pegs, which in many instances put bank bond accounts "in the red" and thus put some penalty on further bank sales, liquidation of bank eligibles dried up and rigid pegs for this area of the market were practically withdrawn. On the second wave of liquidation, beginning in June, selling was concentrated in restricted bonds up to September 8 when the reserve requirement increases were announced. Since then, selling has been generalized and support for bank eligible bonds restored. It will be impossible to say, until data become available some months hence, how the price-supporting in September was divided up between the restricteds and the bank eligibles.

The largest single group of sellers of long-term bonds has been the life insurance companies. Their selling, to accommodate increased lending operations, has greatly accelerated this year over last. The U. S. Treasury survey of ownership of government securities reveals that life insurance companies, which sold \$330 million restricted War Loan 2½s and 2½s during the second half of 1947, sold \$900 more in the first six months of this year. Further heavy sales have been made since June. The life insurance companies have also liquidated bank eligible bonds, and the reduction in their total government security accounts, in the twelve months ended July 31, 1948, is reported by the Institute of Life Insurance at \$2½ billion.

"Inflationary" or "Deflationary"?

A question that cannot be answered at this time is whether the whole gigantic operation of September was on balance "inflationary" or "deflationary". When government bonds are purchased by the Federal Reserve Banks, from member banks who are selling to meet increased reserve requirements, the purchases are not, in the algebra of monetary mechanics, "inflationary". They only undo deflationary effects that increases in reserve requirements would otherwise have.

These technicalities, it is safe to say, are not clear in the minds of most people. The upshot is a good deal of confusion as to what the au-

thorities are about. One of the few clear impressions left in the market is that the authorities have used the occasion to demonstrate an iron-bound determination to keep government bond prices up to established minimum levels.

Another conclusion is that the mechanism of changing reserve requirements is being used quite differently from the way it was first conceived as a mechanism for credit control some fifteen years ago. The problem which then weighed on the minds of the Federal Reserve authorities was that gold inflow from abroad had increased bank reserves to a point where member bank excess reserves were greater than the amount of government securities in the hands of the Federal Reserve Banks. It was calculated that even if the Federal Reserve Banks sold out all the government securities in their open market account the member banks would still have substantial excess reserves as a basis for loan expansion. Thus in the Annual Report of the Federal Reserve Board for 1935 (pp. 13-14) it was stated:

Because of developments previously explained, excess reserves increased from \$800,000,000 to about \$3,000,000,000, while the portfolio of Government securities of the Federal Reserve banks remained at \$2,400,000,000. It is partly for this reason that Congress gave to the Board the power to absorb excess reserves through increasing reserve requirements . . .

In its Annual Report for 1937, after reserve requirements had been placed at double the old statutory rates, the Board wrote (p. 1):

Further adjustment of the country's reserve structure to the changed conditions that have resulted from a heavy inflow of gold from abroad was made by the System in the early part of the year through a final increase of reserve requirements for member banks. This placed the System in a position to make current adjustments to developments in the credit situation through open market operations.

The Federal Advisory Council, in recommending increases in reserve requirements in February, 1936, added this qualification:

The Council wishes to make it clear that it does not believe that reserve requirements should be varied at frequent intervals or except for grave reasons. It is of the opinion that frequent changes in reserve requirements would destroy confidence both on the part of the borrower and the banker and restrict employment of bank credit needed for continued business recovery.

Reserve Requirements versus Open Market Operations

It cannot be said now that reserve requirement increases are necessary because the Reserve Banks do not have enough government securities to absorb excess reserves. In July, 1936, when the first increase in reserve requirements

was ordered, member bank excess reserves were \$3 billion while Reserve Bank holdings of government securities were less than \$2½ billion. At the present time member bank excess reserves are under \$1 billion, near a minimum working level, while the Federal Reserve Banks hold government securities of more than \$23 billion. There is thus no question as to the adequacy — or overadequacy — of powers to absorb idle investment funds by open market sales of government securities by the Federal Reserve Banks. The advantage of open market operations lies in their flexibility, day-to-day and hour-to-hour adjustability. Their effectiveness rests on the fact that the market for U.S. government obligations is so broad that almost any investor or investment institution will buy government securities in preference to competing investment opportunities when the price "looks right."

The reason why the Federal Reserve does not engage in open market operations calculated to put pressure on the credit structure is their concern for keeping government security prices stable.

"Orderly Market Conditions"

The difficulties in which the authorities now find themselves had their small beginnings in the spring of 1937 when the Reserve Banks purchased \$200 million long-term government bonds to allay the effects of reserve requirement increases on government bond prices. The Reserve System then publicly accepted a responsibility for maintaining "orderly conditions" in the government bond market. This duty was conceived to be a minor chore; it was not even mentioned in a statement on "Objectives of Monetary Policy" issued later in the same year by the Federal Reserve Board, nor was it mentioned by President Roosevelt in dedicating the Federal Reserve building at Washington in October, 1937. The stress — in the words of President Roosevelt — was on what the Federal Reserve could accomplish, with its broad powers "to affect the volume and the cost of money", towards "the maintenance of more stable employment" and "achieving greater stability of the true value of the dollar."

Under many types of situations — and most notably in case of war — maintenance of "orderly conditions" in the government bond market is a useful if not indispensable function that the Reserve Banks can perform. Influencing changes in bond price levels is also a recognized channel through which Federal Reserve policy is made effective.

But with the vast further increase in the public debt, a conflict of objectives has arisen and the Reserve System has tended to become preoccupied with stabilizing the government securities market. The interpretation of "orderly market conditions" indeed, has been narrowed to a point where, in the extreme case of restricted War Loan 2½s and 2½s, prices have shown no movement at all for three months past. The pegged prices themselves discourage potential buyers, who interpret the necessity for official price support as *prima facie* evidence that the bonds are overpriced. Thus the redevelopment of a genuine two-sided market is frustrated and with it the opportunities of the authorities to apply their open market techniques toward realization of their broader and more vital functions.

It is now appropriate to recall a statement made by the Reserve Board in the 1939 Annual Report, just after the outbreak of the war:

While the System has neither the obligation nor the power to assure any given level of prices or yields for Government securities, it has been its policy in so far as its powers permit to protect the market for these securities from violent fluctuations of a speculative, or panicky nature. Prices of fixed-interest rate securities, including those of the Government, inevitably adjust to changes in long-time interest rates. Consequently, an orderly rise or fall in United States bond prices in response to changes in underlying credit conditions, as expressed in interest rates, does not call for action by the System. Violent temporary movements, however, caused by such circumstances as the shock of the outbreak of European hostilities, make it in the public interest for the System to use its influence toward preventing a disorganized condition in the market.

The Cost of Crop Support

Bumper yields this year of grains, cotton, and other crops have depressed market prices, in some cases below government loan levels, and confront the United States Government with what seems likely to be the greatest test thus far of its program of guaranteed price support. In President Truman's budget message delivered to Congress last January it was stated that —

At the present time, American agriculture is in the best financial condition in history. Agricultural prices in recent months have been at an all-time high — nearly three times the level of 1940. Net farm income in 1947 was approximately 18 billion dollars — three and one-half times the average net farm income in the years 1935-39 . . .

By 1949, net cash outlays for price support and supply programs will be small because agricultural prices on the whole are expected to be above support levels, and reimbursements from other agencies and cash-paying foreign governments should offset expenditures for procurement of agricultural commodities.

Because of recent changes in the crop and price outlook, however, it now appears that this

government liability for loans and purchases may become one of very great magnitude and a serious threat to the federal budget surplus estimated for this year.

Under the price support legislation, which was recently extended by Congress with some amendments to the middle of 1950, the Department of Agriculture, working through the Commodity Credit Corporation, is directed to give mandatory support to the prices of specified crops, plus permissive support to practically all other agricultural commodities. This support is given in the form of non-recourse loans or outright purchases when the price of any particular commodity approaches or falls below 90 per cent of its computed "parity". "Parity", in turn, is based upon the relationship in some base period between the price that farmers receive for that product and the prices they pay for goods bought from others.

Both the scope and cost of the government operations in this field are difficult to determine. This is because of the large turnover of funds involved, and the fact that the Commodity Credit Corporation—in addition to its price support program—purchases commodities for the E.C.A. and for other agencies, and is engaged also in a foreign purchase program of commodities produced abroad and needed here. Thus most of its "receipts" from other agencies or from "cash-paying foreign governments" reflect expenditures charged in other parts of the federal budget.

Moreover, the corporation's bookkeeping is necessarily complex. It operates jointly on \$100 million capital, and the authority to borrow up to \$4½ billion at any one time from the Treasury, and on loans (government guaranteed) from private lenders, plus \$500 million appropriated by Congress as a reserve against which losses are charged. Furthermore, account must be taken of the changes in outstanding loans and unsold commodities on hand, adjustments in reserves, etc.

In the accompanying summary are shown for fiscal 1949 the estimated expenditures and receipts, and their effect on the government budget, condensed from the detailed tables and text devoted to the C.C.C. in the President's Budget of last January, pages 1149-1176.

It will be seen from this statement that under the crop support program the outlays for commodity loans and purchases were estimated at approximately \$1.5 billion, but that receipts from repayments and sales were estimated at \$1.4 billion, leaving an expenditure excess of only \$114 million. On an overall basis, including the sup-

ply program and the foreign purchase program, and also the operating expenses and other receipts, total operating outlays were estimated at \$3.4 billion against receipts of \$3.3 billion, leaving a net outlay of \$106 million.

U. S. Department of Agriculture—Commodity Credit Corporation

Condensed Summary of Estimated Expenditures and Receipts, and Effect on the Federal Budget, in Fiscal Year Ending June 30, 1949

Price Support Program	Expenditures	Receipts
Loans against commodities*	\$1,138,600,000	
Loan repayments*		\$1,037,535,000
Purchases of commodities	885,573,000	
Sales of commodities		322,285,000
Subtotal—price support	1,474,173,000	1,359,820,000
Supply Program		
Purchases of commodities	1,686,387,000	
Sales of commodities		1,776,349,000
Foreign Purchase Program		
Purchases of commodities	123,590,000	
Sales of commodities		129,790,000
Carrying charges & related expenses	75,294,000	
Administrative expenses	22,724,530	
Miscellaneous expenses	13,409,700	
Service receipts from other agencies		15,149,530
Miscellaneous receipts		13,574,000
Grand total from operations	3,400,578,230	3,294,682,530
Excess of operating expenditures	105,895,700	
C.C.C. Borrowings & Repayments		
Borrowings from U.S. Treasury		1,070,000,000
Borrowings from private lenders		90,000,000
Repayments to U.S. Treasury	1,147,015,000	
Repayments to private lenders	92,000,000	
Grand total of funds applied	4,639,593,230	4,454,682,530
Decrease in working capital		184,910,700
Effect on the Federal Budget		
Checking account expenditures	3,398,788,230	
Total corporate receipts		3,384,682,530
Redemption of public obligations		2,000,000
Net budget expenditures	12,105,700	
Savings from revised legislation		50,000,000
Net budget receipts		37,894,300

*Includes \$37,635,000 loan to and repayment by the Secretary of Agriculture for conservation purposes.

By reducing holdings of commodities, however, and using the proceeds to repay loans, it was estimated that the net drain of the C.C.C. upon the Treasury this year would be reduced to only \$12 million. Moreover, it was calculated that the revision in the legislation extending the parity support program would result in a saving of \$50 million, so that, surprisingly enough, the C.C.C. operations would end up with net receipts of \$38 million. This figure, given in the official budget submitted to Congress last January, was repeated in the revised estimates issued in August. At that time the President stated:

The Congress enacted a more flexible price support program, such as I recommended, but postponed its effective date. This postponement will result in increased expenditures during the fiscal year 1949 above those estimated in January. This increase will be offset, however, by larger repayments on commodity loans than were previously anticipated. Increases in prices paid by farmers during the past year and a half, coupled with decreases in prices received by farmers for some agricultural commodities, such as wheat, cotton and potatoes, have narrowed or eliminated the margin between market

prices and minimum support levels. Under these circumstances, expenditure estimates in this field must be regarded as tentative.

In the light of the further improvement that has taken place in crop prospects, and of the already heavy outlays that have been necessary for price support, this predicted surplus appears exceedingly optimistic. While the entire Department of Agriculture budget totals \$868 million, including \$38 million receipts from the C.C.C., the changed picture is likely to result in considerably greater expenditures for agriculture.

Outlays by Commodities

Aside from those people engaged in the business of food production, processing and distribution, the public has become familiar with the price support program only recently because of its effect in holding up living costs and the problem of checking inflation. Even now, however, relatively few people probably realize the scope of this program.

The accompanying table shows by individual commodities for fiscal 1949 the C.C.C. estimates under the price support program as presented in January.

U. S. Department of Agriculture — Commodity Credit Corporation

Estimated Commodity Loans, Repayments, Purchases, and Sales Under the Price Support Program in Fiscal Year Ending June 30, 1949

(In Millions of Dollars)

Basic commodities:	Loans		Commodities	
	New Loans	Repayments	Purchases	Sales
Corn	\$150	\$ 51	\$ —	\$ —
Cotton	362	245	—	3
Peanuts	43	43	\$2	28
Rice	9	9	—	—
Tobacco	66	195	—	—
Wheat	200	202	—	—
Steagall commodities:				
Beans, dry edible	•	•	—	•
Cotton, Amer.-Egypt...	•	•	—	•
Eggs	—	—	38	50
Flaxseed	25	25	50	51
Potatoes, Irish	91	87	\$2	4
Potatoes, sweet	—	—	7	2
Soybeans	108	108	4	5
All other commodities:				
Barley	17	17	—	—
Oats	1	1	—	—
Rye	1	1	—	—
Flax, fibre	—	—	—	•
Hemp	—	—	—	•
Seeds, hay and pasture	—	—	4	4
Seeds, winter cover crop	—	—	•	2
Wool	—	—	168	174
Rosin	10	—	—	—
Turpentine	2	—	—	—
Sorghums, grain	13	13	—	—
Total	\$1,101	\$1,000	\$336	\$822
Excess of expenditures		101		13

*Not over \$500,000

It will be seen that while the outlays, exclusive of operating and administrative expenses, were estimated at over \$1.4 billion, it was expected that for every \$10 paid out more than \$9 would be recovered, leaving only a relatively small net

outlay and actually giving, after adjustments, a Treasury surplus. With record harvests here, and large crops in other countries exerting pressure upon prices, however, the estimates are now subject to five major uncertainties. These are (1) how large the total of non-recourse loans at fixed prices the C.C.C. may have to make with some markets already below such prices, (2) how many of these loans the borrowers will choose to repay if market prices remain depressed, (3) how large the outright commodity purchases may have to be to support prices, (4) how much of such commodities can be disposed of, in view of both legal and practical limitations, if market prices remain below support levels, and (5) what losses will have to be taken on loans and on commodities acquired.

Recent Trends in Outlays

As an example of recent changes in crop and price outlook, indicating substantial expansion in the government contingent liability for price support, the New York Times of September 22 carried the following dispatch from Washington:

Growers of two major oil-seed crops — soy beans and flaxseed — received new assurances from the Government today of support prices for these products. Because of big yields of these crops, prices have tended to drop below the levels promised by the Government.

In a formal announcement the Department of Agriculture said it will take "all necessary steps" to carry out the Government's price guarantee of \$6 a bushel for No. 1 flaxseed, Minneapolis basis. It announced also that loans will be made to growers on soy beans, whether stored on the farm or in commercial warehouses, at the price support rate of \$2.18 a bushel.

The problem of supporting prices of oil seeds has been complicated by the fact that most processors have withdrawn from the market. They say they cannot pay the price support rates and come out on the oil-seed by-products.

"We are moving several million bushels of flaxseed into export position on the Eastern seaboard," the department announced. "We have also arranged for enough country and terminal storage facilities to handle the situation."

Thus in the case of flaxseed, one of the less important farm crops, the Department of Agriculture has since announced that through September 23 it has had to purchase 17 million bushels at a cost of \$102 million, whereas the budget estimate for the full fiscal year was for no net outlay whatever. To the extent that the C.C.C. can export the "surplus", either by sale, or by transfer of the charge to the "International Affairs and Finance" section of the budget, its own funds may of course be recouped and its loss on the operation minimized. This, however, is just a case of putting money from one pocket to another. It all comes out of the American taxpayer. It might be added that linseed oil, made from flaxseed, has throughout the war

period and until very recently been extremely scarce; this has been a factor in the scarcity and high prices of paint and linoleum, of which it is a principal ingredient.

In the case of soybeans, the recent start to the harvesting of a bumper crop (205 million bushels, against the ten-year average of 135 million) has caused a sharp break in prices. Soybeans sold early this year for \$4.43 per bushel, a record high, but are now down around \$2.35, approaching the loan rate of \$2.18. Yet the budget indicated that no net outlay would be required for price support.

With a cotton crop of over 15 million bales, the largest in eleven years, and the price down around the support level of 30.74 cents per pound (compared with the 1948 high of 39.35, and the 1939 average of 8.70) growers may, instead of selling their crop into trade channels, either turn in from 3 to 6 million bales against government "loans" where it will be held off the market unless they choose to redeem it by July 31, 1949, or else contract for direct sale to the C.C.C. This would require some \$450 to \$900 million of C.C.C. funds, whereas the net outlay estimated for cotton was but \$114 million.

Such "loans", made at inflated prices and repayable only at the option of the borrower unless the price goes up, are in effect simply a joint gamble by the grower and the Government on the future course of the markets. If the price does go up, the grower wins, but if it goes down, the Government loses, which means the taxpayer. Meanwhile, the cotton is withheld from industry, where it might help to lower clothing prices.

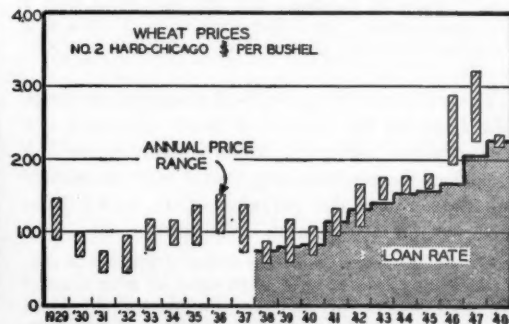
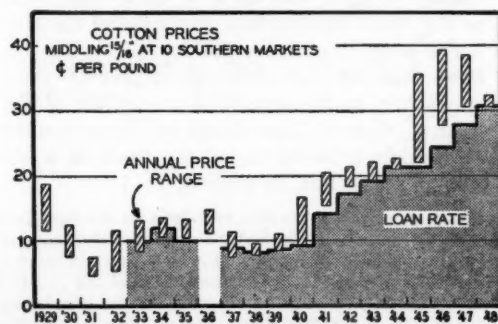
A near-record wheat crop of almost 1.3 billion bushels might mean that 200 to 400 million bushels would be turned into the C.C.C. at the support price of \$2.00, which would also call for an outlay ranging from \$400 to \$800 million. Of

this year's crop, 90 million bushels had already gone into the loan and 8 million had been purchased by August 31. In the budget it was estimated that \$2 million credit would be obtained on wheat.

Estimates for the corn crop have now been raised to over 3.5 billion bushels, an all-time high record. It now appears that much of the corn crop cannot be made eligible for the loan because the necessary storage space cannot be found. But if 300 to 500 million bushels should be taken over by the Government at \$1.45, this would involve an outlay of \$400 to \$700 million. The budget estimated only \$99 million.

Similar examples could be cited for other farm products. Conditions might change, of course, so as to reduce the portion of crops that the Government will have to take over as loan collateral or as outright purchases, or to increase loan repayments and disposal of commodities. In the case of cotton, corn, and peanuts, the C.C.C. drain upon the Treasury might be postponed to the succeeding year if loans remain outstanding. Also, the cost of increased C.C.C. purchases might be shifted to an enlarged E.C.A. food program, such as has been urged by Secretary of Agriculture Brannan as a means of disposing of some of the prospective crop surpluses.

On the other hand, conditions might change in the other direction, so as to require even greater net outlays to keep prices up. Because of the fact, illustrated by the chart, that the guaranteed "parity" prices have been moved up automatically during the period of wartime and postwar inflation, in which farm products soared higher than any other major group, the potential liability under the government support program, just beginning to be realized generally, may run into many billions of dollars.



Annual Range of Raw Cotton and Wheat Prices, Compared with Government Support Prices, by Crop Years. (1948 prices through September only.)

"Whither Bound?"

Taking the above question as text for an address in Manchester, England, this past summer, Sir John Anderson, M.P., formerly Chancellor of the Exchequer in the Churchill Government, had some things to say about the doctrines and practices of socialism in Great Britain today that merit carrying to a larger audience. Though Sir John was speaking to a group of British business men, about British affairs, his remarks have far wider application. Everywhere people are asking the same question, "Where are we, and what are we heading for?", and the theories which Sir John feels are befuddling and misleading the British people have their advocates in every country.

Sir John minces no words. "I think the answer is that we are in a fool's paradise, in a world of illusion, and that we are heading for disaster." While disclaiming any belief that disaster is inevitable, and declaring his faith in the British people, he nevertheless warned that "the abyss is yawning not very far ahead and a quick manoeuvre will have to be executed to avoid it."

Sir John mentions four characteristics of this "fool's paradise", and puts first "the prevalence of false doctrines, and notably the false doctrine of equality."

Doctrine of "Equality"

We are here, he said, in the presence of a fallacy which is very widespread and very far reaching. Pointing out that he was referring to economic equality, he described this doctrine as involving the view that —

it must be right to take by taxation from those who have more than the average not merely for the common services of the community but just to effect a more equal distribution. You hear that doctrine in this form enunciated from time to time by leading statesmen, e.g. by my immediate successor as Chancellor of the Exchequer and by the President of the Board of Trade. They use it to justify measures which, in my view, are little better than legalized brigandage, saying, "Oh well, when it is done he (the taxpayer in question) will still have more than a great many others," as if that were relevant when it is a question of taking what you are not entitled in justice to take.

The fact that the process of taking from those who have for the benefit of those who have not means often taking from the deserving for the benefit of the undeserving, that it may encourage the slacker and the parasite — that, as Sir John observes, "is all ignored." He continued:

The fallacy keeps constantly cropping up, and is constantly sought to be justified by an attack on what is called the profit motive. Mr. Morrison [President of the Board of Trade, in England a government office], a gentleman for whom I have a great respect — though he makes un-

guarded utterances at times — said this the other day: "Socialism is the only moral policy because it rejects the profit motive."

What nonsense! Is it too much to say, what hypocrisy? The profit motive in one form or another will never be discarded as long as man walks this earth.

Are we not all governed by it? Does it not in truth provide the momentum behind the main objects of socialist policy — nationalization and so on?

Don't they derive from the idea that they will benefit those who vote for them? I dare say you will have noticed that Mr. Horner — the Mineworkers Union — claimed as reforms, he called them reforms, for the benefit of the workers since the nationalization of the mines, the equivalent of £80,000,000 and he said that there was more to come. Is there no profit motive there? Can anyone deny that the profit motive is the most powerful governing impulse in human conduct? Is there anything disgraceful about it? Is the desire to better oneself something one should be ashamed of, particularly when it flows from a most laudable desire to better those who are dependent on one — one's friends and relatives?

Here the speaker makes the point that there can never be full equality in this world. Indeed, full equality would lead to stagnation. He says:

Actually, I assert that economic equality if we could achieve it, which we never will — we may suffer from the attempt — would inevitably mean stagnation and death. The dependence of progress upon the existence of inequalities is a fundamental law of nature which cannot be wholly inhibited so long as any vestige of individual freedom remains.

The process, he asserted, of attempting to raise the standards of the community as a whole by merely securing a more equitable distribution of this world's goods —

not only destroys incentive but, and this is much more serious, it obscures the fact that much greater exertion all round is what is needed to repair the ravages of the war before there can be any question of improved standards.

What do we see? We have seen during the past two and a half years higher wages, shorter hours, longer holidays with pay, family allowances, heavy expenditures on social insurance, a longer period of schooling, and artificial reduction in living costs for all.

Illusion of the "New Policy"

Acknowledging that most of these things may be very good in their way, and most of them are in the program of every political party, Sir John views them as part of the great illusion, which brings him to the second characteristic of that illusion, "that all these things are thought to be, and widely believed to be, the fruits of a new policy." As to this, he replied:

In fact, all this is possible only because we have been living on charity. In the first place we had the American loan, a large sum of money, all gone — I do not say frittered away — but gone. And now Marshall aid . . . It is not so much a question of whether we can afford these things . . . as whether their existence does not confirm people in their wrong ideas.

Citing the dockers' strike at that time crippling the Port of London, he goes on to say:

Since the beginning of the last war dock labor, which was casual, has been completely de-casualized. The remuneration of dockers as permanent laborers was based on rates negotiated from the standpoint of casual labor. That in itself was a gain.

But on top of that there have been various increases. Dockers themselves are compelled to recognize that their economic situation has changed out of all knowledge. They have been clamoring with others for nationalization for several years. They are now completely nationalized. They are all employed by a body called the National Dock Labour Corporation in the control of which they have a very considerable share.

They are guaranteed a minimum wage and regular employment. What are they asked to give in return? A reasonable measure of discipline. And at the first attempt to enforce such discipline at the instance of their own leaders they repudiate it all and inflict incalculable loss on the community, on the shipping and dock interests which are not involved in any way in this dispute, and which are quite helpless.

These men, concludes Sir John, cannot possibly realize what is involved. Because of the prevalence of false doctrine referred to above, the truth has not been brought home to them. Somehow a change of outlook is essential. How is it to come about?

"There are indeed welcome signs in the recent utterances of men like Morrison and Cripps, and among trade union leaders like Jack Tanner." But Sir John is skeptical "whether any mere words will be sufficient to counteract the effect of false doctrines that have been sedulously propagated for many years."

Will the change mean that the progress "of what may be called social evolution" will be set back, or held up indefinitely? "Not necessarily". Citing the long record of social legislation under Tory Governments, the speaker asks his hearers to bear in mind that such measures "are not by any means the monopoly of any political party."

Danger in Great Haste

The great difference between the Socialistic administration and a Conservative or Liberal administration, in the opinion of Sir John, is that "the Socialists want to rush at everything at breakneck speed."

This tendency to hasty change, he said, is the "third characteristic" of the times, and involves grave danger:

In a free democracy laws must have the backing of the great majority in the community. It is not enough that they should be passed by a narrow majority, unless, once they reach the Statute Book, they are accepted by the community as a whole, as fair and reasonable . . .

A great statesman, Field Marshal Smuts, said the other day in Cambridge that he thought the whole world was passing through a period of great secular change. He thought that that was something which was happening quite apart from the war. What he meant I am sure was that war might be described as a great solvent, that in a state of war existing systems and relationships go into solution and then re-crystallize in a new form.

Unless this is recognized, and unless the process of change is deliberately slowed down, things may happen that are so far ahead of public opinion that they lead to intellectual resistance or even open revolt.

And in that, gentlemen, there is always the danger of Socialism giving place to some more authoritarian system, what Mr. Attlee called "bureaucratic collectivism."

That also, gentlemen, is why some people even doubt whether Socialist rule, as distinct from a progressively increasing measure of practical Socialism — and I make that distinction — is in the long run consistent with true democracy.

Faith in the Planned Economy

The fourth characteristic of this world of illusion that Sir John talks about is "a pathetic belief, widely prevalent, in the capacity of human beings to plan in detail the life of a free community."

There disillusion "is coming fairly quickly", for—

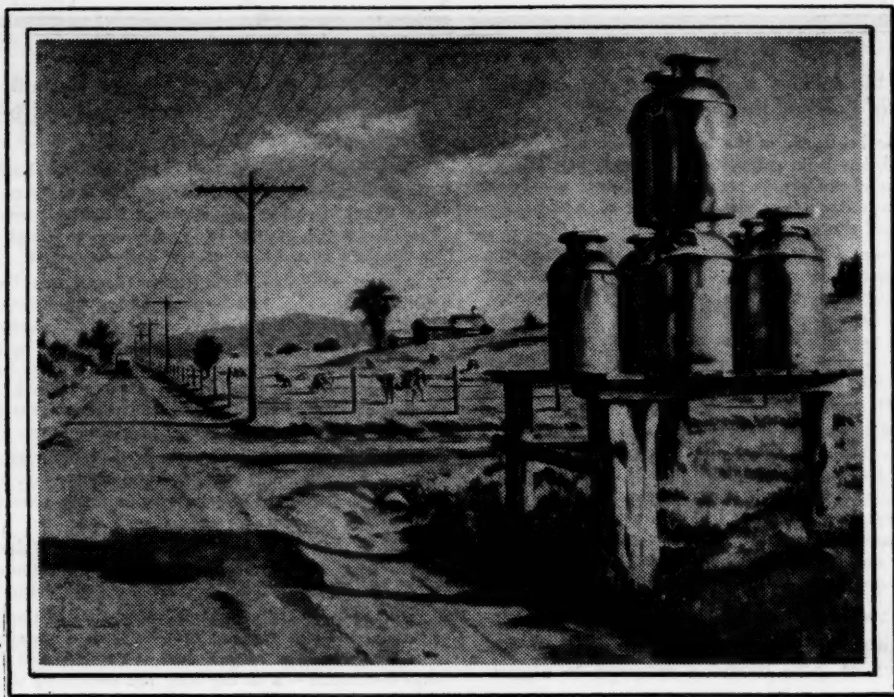
Conscious planning by people in offices, playing about with statistics that are always largely out of date, inevitably, can never take the place of the instinctive mental processes of people brought up in the businesses they are carrying on.

In concluding his address, Sir John referred to the difficulties facing all Western European countries and to the grave problems of international relations:

We must bring these international questions to issue so that all men see clearly where they stand and so that if danger threatens the people concerned may be adequately informed and led to take whatever measures are necessary to guard against it.

That is our problem, but not ours alone. We shall not, in my opinion, solve it, or any of our other great problems, without a much higher measure of unity in the direction of our national affairs than we have now.

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